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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

March 31, 2007

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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

March 31, 2007

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APPOINTIVE OFFICIALS

George Parisot, Lottery Director

John Tarr, Lottery Assistant Director for Security

LOTTERY COMMISSION		TERM EXPIRES
Tom Keegan	Helena	January 1, 2010
Beth O'Halloran	Missoula	January 1, 2010
Robert Crippen	Butte	January 1, 2011
Wilbur Rehmann	Helena	January 1, 2009
Craig Anderson	Glendive	January 1, 2009

According to Section 23-7-202(9), MCA, copies of this report must be distributed to the following:

Governor – Brian Schweitzer
Director of Dept. of Administration – Janet Kelly
Legislative Auditor - Scott Seacat
President of the Senate – Mike Cooney
Speaker of the House – Scott Sales

The law also states "the President of the Senate and the Speaker of the House will determine the report distribution to each member of the appropriate committee of each house of the legislature". The President of the Senate and the Speaker of the House have requested that this report be distributed to the following committees:

HOUSE – State Administration Committee

Dennis Himmelberger, Chair
Duane Ankney, Vice Chair (R)
Hal Jacobson, Vice Chair (D)
Debby Barrett
Gary Branae
Mary Caferro
Sue Dickenson
Gordon Hendrick
Teresa Henry
Pat Ingraham
Bill Jones
Bruce Malcolm
Walter McNutt
Alan Olson
Mike Phillips
Scott Sales
Veronica Small-Eastman
Frankie Wilmer

HOUSE – Business & Labor Committee

Scott Mendenhall, Chair
Mike Milburn, Vice Chair (R)
Jim Keane, Vice Chair (D)
Elsie Arntzen
Shannon Augare
Scott Boggio
Ernie Dutton
Kevin Furey
Ralph Heinert
Llew Jones
Harry Klock
Michele Reinhart
Wayne Stahl
Bill Thomas
Kendall Van Dyk
Jonathan Windy Boy

SENATE – State Administration Committee

Carolyn Squires, Chair
Joe Balyeat
Vicki Cocchiarella
Jeff Essmann
Steve Gallus
Larry Jent
Rick Laible
Jesse Laslovich
Dave Lewis
Jim Shockley
Joe Tropila

SENATE – Business, Labor, & Economic Affairs Committee

Vicki Cocchiarella, Chair
Joe Balyeat
Roy Brown
John Esp
Verdell Jackson
Lane Larson
Don Ryan
Frank Smith
Carolyn Squires
Donald Steinbeisser
Joe Tropila

June 2007

Montana Lottery Commission:

The Lottery will transfer $3,183,910 to the General Fund as a result of operations in the third quarter of fiscal year 2007 compared to $2,499,413 for the same period last fiscal year. Total transfer this fiscal year will be $8,566,729. This transfer represents 88 % of the total budget. The percent of transfer to total operating revenue for this quarter is at 28% compared to 23% for the quarter last year and 27% overall for this fiscal year compared to 21% last fiscal year.

All products except Powerball experienced increased sales over last year. Powerball sales have decreased by 11%. Scratch sales up by 8%. Wild Card's sales have increased by 23%. Hot Lotto sales were up by 29%. Montana Cash increase by 13% and Quik Tix has increased by 22%. Overall, sales were up 4% over last year.

Direct game costs were consistent with sales for the quarter except for Vendor Fees, which are reduced due to the new contract. Net operating revenue as a percent of total revenue is 35% for the quarter compared to 32% last year. Total operating expenses of $765,691 for the quarter are lower than last year's by 30%, because of reduced depreciation and amortization.

We expect a busy summer with an events schedule that will provide us another opportunity to visit our players and retailers. As we've seen in the past, this outreach effort coupled with exciting new scratch games should be a benefit for the Lottery's bottom line.

Sincerely,

George Parisot
Director

2525 North Montana Avenue • Helena MT 59601-0598
Phone 406-444-LUCK (5825) • Fax 406-444-5830

MONTANA LOTTERY
STATEMENT OF NET ASSETS
MARCH 31, 2007 and 2006
(UNAUDITED)

	Period Ended March 31, 2007	Period Ended March 31, 2006
ASSETS:		
CURRENT ASSETS		
Cash and Cash Equivalents	$ 3,149,163	$ 3,055,511
Receivables (Net)	1,433,324	1,107,870
Inventories	1,200,331	637,973
Other Current Assets	8,238	13,201
TOTAL CURRENT ASSETS	5,791,056	4,814,555
NONCURRENT ASSETS		
Computer, Furniture & Equipment	455,284	5,613,010
Accumulated Depreciation	(308,640)	(5,480,201)
Multi-State Receivable	1,486,396	1,351,649
TOTAL NONCURRENT ASSETS	1,633,040	1,484,458
TOTAL ASSETS	$ 7,424,096	$ 6,299,013
LIABILITIES:		
CURRENT LIABILITIES		
Accounts Payable	$ 313,246	$ 383,335
Estimated Prize Liability	2,391,759	1,771,465
Due to Primary Government	2,279	3,657
Transfer Obligations	3,183,910	2,499,413
Deferred Revenue	102,210	184,461
Current Portion Comp. Absences	111,176	129,147
TOTAL CURRENT LIABILITIES	6,104,580	4,971,478
NONCURRENT LIABILITIES		
MUSL Prize Liability	1,239,942	1,264,434
Accrued Compensated Absences	79,574	63,101
TOTAL NONCURRENT LIABILITIES	1,319,516	1,327,535
TOTAL LIABILITIES	7,424,096	6,299,013
NET ASSETS		
Unrestricted Net Assets	0	0
TOTAL LIABILITIES AND NET ASSETS	$ 7,424,096	$ 6,299,013

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
FOR THE QUARTERS ENDED MARCH 31, 2007 and 2006
(Unaudited)

	Quarter Ended March 31, 2007	Quarter Ended March 31, 2006	Nine Months Ended March 31, 2007	Nine Months Ended March 31, 2006
OPERATING REVENUES:				
Scratch ticket revenue	$ 3,359,164	$ 2,885,650	$ 9,419,796	$ 8,669,389
Powerball revenue	4,752,340	5,598,560	13,237,162	14,665,252
Montana Cash revenue	1,238,125	1,040,606	3,610,160	3,126,171
Wild Card revenue	907,682	629,705	2,276,460	1,755,203
Hot Lotto revenue	922,985	836,244	2,996,181	2,113,629
Qwik Tix revenue	113,565	91,787	356,001	276,302
License, permits, and misc	400	620	2,555	1,865
Total Operating Revenues	11,294,261	11,083,172	31,898,315	30,607,811
Less Direct Game Costs:				
Scratch ticket prize expense	(1,984,362)	(1,725,388)	(5,757,025)	(5,250,363)
On-line ticket prize expense	(3,916,851)	(4,072,874)	(10,946,841)	(10,786,964)
Retailer commission	(660,913)	(634,679)	(1,884,854)	(1,808,597)
Cost of tickets sold	(176,559)	(193,058)	(629,339)	(696,832)
Vendor fees	(656,140)	(927,862)	(1,901,195)	(2,562,224)
Net Operating Revenue	3,899,436	3,529,311	10,779,061	9,502,831
OPERATING EXPENSES:				
Advertising	149,202	136,934	458,902	398,046
Advertising Production	17,274	115,144	91,089	183,508
Audit Fees	2,653	19,505	27,530	61,602
Bad Debts Expense	0	0	1,073	(45)
Communications	24,176	23,194	67,345	65,518
Contractual Services	22,339	22,542	62,578	90,775
Depreciation and Amortization	8,243	247,646	22,578	783,576
Interest Expense	0	0	0	0
Administrative Service Fee	13,504	13,486	40,511	40,457
State Cost Recovery	1,694	1,608	1,694	2,412
Multi-State Dues	(4,000)	0	2,077	72,333
Public Relations	15,670	4,344	61,753	12,987
Other	14,450	9,598	30,160	26,115
Personal Services	414,464	412,820	1,215,346	1,227,015
Repairs and Maintenance	4,510	4,573	10,094	8,774
Supplies and Materials	45,083	43,060	146,836	140,718
Travel	7,115	10,400	32,393	30,618
Utilities and Rent	29,314	30,401	84,976	85,816
Total Operating Expense	765,691	1,095,255	2,356,935	3,230,225
Operating Income	3,133,745	2,434,056	8,422,126	6,272,606
NONOPERATING REVENUES (EXPENSES)				
Interest earnings	50,165	65,357	144,603	128,379
Total Nonoperating Revenues(Expenses)	50,165	65,357	144,603	128,379
Income Before Operating Transfers	3,183,910	2,499,413	8,566,729	6,400,985
Operating Transfers In (Out) - General Fund	(3,183,910)	(2,499,413)	(8,566,729)	(6,400,985)
Total Operating Transfers Out	(3,183,910)	(2,499,413)	(8,566,729)	(6,400,985)
CHANGE IN NET ASSETS	0	0	0	0
Total Net Assets, Beginning of Period	0	0	0	0
TOTAL NET ASSETS, END OF PERIOD	$ 0	$ 0	$ 0	$ 0

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN NET FUND ASSETS
AND RECONCILIATION OF BUDGET AND ACTUAL (BUDGETARY BASIS) TO GAAP BASIS
FOR THE NINE MONTHS ENDED MARCH 31, 2007
(Unaudited)

	Budget Fiscal Year July 1, 2006 - June 30, 2007	Actual Nine Months Ended March 31, 2007 (Unaudited)	Actual as a Percent of Final Budget (%)
REVENUES:			
Scratch ticket revenue	$ $11,000,000	$ 9,419,796	85.63
Powerball revenue	19,500,000	13,237,162	67.88
Montana Cash revenue	3,800,000	3,610,160	95.00
Wild Card revenue	2,100,000	2,276,460	108.40
Hot Lotto revenue	2,500,000	2,996,181	119.85
Qwik Tix revenue	350,000	356,001	101.71
License, permits, and miscellaneous	2,000	2,555	127.75
Total Revenues	39,252,000	31,898,315	81.27
DIRECT GAME COSTS:			
Prizes - Scratch ticket	6,490,000	5,757,025	88.71
Prizes - Lotto games	14,021,000	10,734,391	76.56
Prizes - Qwik Tix	210,000	212,450	101.17
Retailer commissions	2,303,000	1,884,854	81.84
Ticket cost - scratch games	990,000	629,339	63.57
Ticket cost - vendor fees	2,286,500	1,901,195	83.15
Total Direct Game Costs	26,300,500	21,119,254	80.30
OPERATING EXPENSES:			
Advertising	602,750	458,902	76.13
Advertising Production	159,500	91,089	57.11
Audit Fees	35,000	27,530	78.66
Communications	83,319	67,345	80.83
Contractual Services	134,808	62,578	46.42
Administrative Service Fee	55,000	40,511	73.66
State Cost Recovery	3,143	1,694	53.90
Multi-State Dues	92,566	2,077	2.24
Public Relations	67,520	61,753	91.46
Other	50,712	30,160	59.47
Personal Services	1,655,639	1,215,346	73.41
Repairs and Maintenance	12,470	10,094	80.95
Supplies and Materials	195,125	146,836	75.25
Travel	45,448	32,393	71.27
Utilities and Rent	120,080	84,976	70.77
Equipment	38,839	43,614	112.29
Total Operating Expenses	3,351,919	2,376,898	70.91
Operating Income	9,599,581	8,402,163	87.53
NONOPERATING REVENUES (EXPENSES):			
Court Settlements	0	0	
Interest Earnings	100,000	131,025	
Security Lending Transactions		0	
Gain/(Loss) on Sale on Asset		0	
NET INCOME (BUDGETARY BASIS)	$ 9,699,581	$ 8,533,188	87.97
RECONCILIATION OF BUDGETARY/GAAP BASIS:			
1. Capitalized equipment purchases	38,839	43,614	112.29
2. Adjustment for compensated absences		0	
3. Adjustment for depreciation expense	(35,000)	(22,578)	64.51
4. Bad Debts		(1,073)	
5. MUSL interest earnings	50,000	13,578	27.16
Total Reconciling Items	53,839	33,541	
NET INCOME (GAAP BASIS)	$ 9,753,420	$ 8,566,729	87.83

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
ANALYSIS OF REVENUES AND EXPENSES BY PRODUCT
FOR THE QUARTER ENDED MARCH 31, 2007
(UNAUDITED)

	SCRATCH	POWERBALL	MONTANA CASH	WILD CARD	HOT LOTTO	QWIK TIX	ADMIN
REVENUES:	$ 9,419,796	$ 13,237,162	$ 3,610,160	$ 2,276,460	$ 2,996,181	$ 356,001	$ 2,555
DIRECT GAME COSTS:							
Prize Expense	5,757,025	6,185,905	1,886,731	1,208,844	1,452,911	212,450	0
Retailer Commissions	761,331	661,683	180,483	113,791	149,789	17,777	0
Cost of Tickets Sold	629,339	0	0	0	0	0	0
Vendor Fees	565,683	779,215	215,406	137,819	179,592	23,480	0
NET OPERATING REVENUE	1,706,418	5,610,359	1,327,540	816,006	1,213,889	102,294	2,555
OPERATING EXPENSES:							
Advertising	195,062	194,709	22,209	21,933	21,014	1,516	2,460
Advertising Production	53,152	24,366	4,523	4,525	4,523	0	0
Audit Fees	0	0	0	0	0	0	27,530
Bad Debts	0	0	0	0	0	0	1,073
Communications	39,263	57	57	57	57	57	27,798
Contractual Services	641	276	277	277	277	922	59,908
Depreciation and Amortization	11,988	4,076	1,918	1,199	1,199	999	1,199
Interest	0	0	0	0	0	0	0
Administrative Service Fee	9,569	4,270	3,662	2,512	2,491	2,127	15,880
State Cost Recovery	0	0	0	0	0	0	1,694
Multi-State Dues	0	(4,946)	0	20,473	(1,529)	0	(11,922)
Public Relations	7,913	9,122	9,122	9,122	9,122	9,122	8,231
Other	1,921	99	99	99	99	0	27,842
Personal Services	387,632	132,651	105,487	65,329	64,594	54,729	404,924
Repairs and Maintenance	0	0	0	0	0	0	10,094
Supplies and Materials	44,824	(521)	(475)	(521)	(521)	(1,258)	105,308
Travel	0	16	16	16	16	0	32,329
Utilities and Rent	0	0	0	0	0	0	84,976
TOTAL OPERATING EXPENSES	751,965	364,175	146,895	125,021	101,342	68,214	799,324
OPERATING INCOME	954,453	5,246,184	1,180,645	690,985	1,112,547	34,080	(796,769)
NONOPERATING REVENUES (EXPENSES)							
Security Lending Transactions	0	0	0	0	0	0	0
Interest Earnings	0	0	0	0	0	0	144,603
[illegible]n(Loss) on Sale of Asset							0
[illegible]ocioeconomic impact of Gambling Stu	0	0	0	0	0	0	0
TOTAL NONOPERATING REVENUES ENSES)	0	0	0	0	0	0	144,603
NET INCOME BY F	$ 954,453	$ 5,246,184	$ 1,180,645	$ 690,985	$ 1,112,547	34,080	$ (652,166)
PROFIT AS A % OF REVENUE	10.13%	39.63%	32.70%	30.35%	37.13%	9.57%	N/A

NOTE: THIS IS ONLY NINE MONTH'S ACTIVITY AND THEREFORE SHOULD NOT BE INTERPRETED TO SHOW HOW OUR PRODUCTS HAVE PERFORMED IN PAST YEARS OR WILL PERFORM IN THE FUTURE.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity.

The Montana Lottery, established under the provisions of Section 23-7-101, Montana Code Annotated (MCA), was approved by the Montana electorate through Legislative Referendum No. 100 on November 4, 1986.

Montana's first lottery tickets went on sale June 24, 1987.

The Montana Lottery is operated by a five-member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the types and forms of lottery games, set the ticket price, number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games in conjunction with other lottery states and countries, and prepare financial reports. The Montana Lottery is attached to the Montana Department of Administration for administrative purposes.

The Montana Lottery is included as an enterprise fund in the State of Montana's Comprehensive Annual Financial Report. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Montana Lottery's financial statements as a reporting agency.

Basis of Presentation. The Montana Lottery reports its financial activity in accordance with generally accepted accounting principles (GAAP) as prescribed in pronouncements of the Governmental Accounting Standards Board (GASB).

Enterprise Fund. The Montana Lottery is classified as an Enterprise Fund of the Governmental Proprietary Fund Type. Enterprise Funds account for operations: a) financed and operated similar to private business enterprises, where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or b) where the Legislature has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate.

Basis of Accounting. The Montana Lottery's financial statements are prepared using the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

Revenue Recognition. Lottery scratch ticket sales are recorded as revenue based on the time the retailer activates the pack of tickets for sale. In accordance with an established policy, retailers may return unsold tickets to the Lottery for credit. Sales are decreased by an allowance for estimated ticket returns.

Ticket sales for lotto games, Powerball, Wild Card, Montana Cash, and Hot Lotto are recorded as revenue based on drawings. Tickets sold in advance for future drawings are recorded as deferred revenue until such time as the tickets become valid for the most current drawing. Qwik Tix revenue is recognized at the time of sale by the retailers.

Promotional Credits. The Lottery issues promotional credits to retailers to be used to distribute free tickets to players. The tickets are distributed as part of a promotion run by the retailer, e.g., "Ask for the Sale" or second chance drawings. The Lottery also directly distributes scratch tickets for promotional purposes at trade shows, for media give-aways, and during new game introductions. The tickets distributed as a result of promotional credits are reflected as a reduction in revenue. The related prize expense and ticket cost for all promotions are reclassified as an advertising expense. For the quarter ended March 31, 2007, promotional credits resulted in a revenue reduction of approximately $8,338 and an expense reclassification of approximately $7,516. For the nine months ended March 31, 2007, promotional credits resulted in a revenue reduction of approximately $56,847 and an expense reclassification of approximately $43,970.

Prizes. Expenses for scratch prizes are recorded based on the predetermined prize structure for each game. Expenses for lotto and Qwik Tix prizes are recorded based on the predetermined prize structure for each individual game. No prize expense is recorded for free tickets distributed.

Unclaimed Prizes. Prizes for the lotto games must be claimed within six months after the appropriate draw date. Prizes for scratch games must be claimed within six months of the announced end of each game. Qwik Tix prizes must be claimed within six months of the sale date. The unclaimed prize amounts are taken as a reduction in the Lottery Prizes Payable liability and the Prize Expense and are transferred to the State of Montana General Fund as a portion of the quarterly transfer. The amount of unclaimed prizes for all games is represented in the table below.

	Quarter Ended 3/31/07	Quarter Ended 3/31/06	Year To Date 3/31/07	Year To Date 3/31/06
Lotto & Qwik Tix	$149,658	$111,345	$568,004	$426,184
Scratch	118,725	74,156	138,691	147,279
TOTALS	$268,383	$185,501	$706,695	$573,463

2. SUMMARY OF ACCOUNTS

Cash and Cash Equivalents. Cash and cash equivalents consist of interest-bearing deposits with the Montana Board of Investments short-term investment pool, cash on deposit with a bank and cash on deposit with the Montana State Treasurer that is part of the State's pooled cash and is not separately identifiable as to specific types of securities. These funds are highly liquid and may be drawn on daily.

Cash and cash equivalents consist of the following:

	March 31,	
	2007	2006
Short-term investment pool	$2,723,831	$2,897,424
Cash on deposit with State Treasurer	415,182	147,937
Cash in revolving deposit account	10,000	10,000
Petty Cash	150	150
TOTALS	$3,149,163	$3,055,511

Reference to the State of Montana's Comprehensive Annual Financial Report would identify the level of risk associated with cash and cash equivalents in the short-term investment pool and amounts retained with the State Treasurer. The bank balance of the revolving deposit account was $25,249 at March 31, 2007 and was covered by federal depository insurance. The carrying amount reported in the balance sheet for cash and cash equivalents approximates the fair market value.

Receivables. Receivables include $1,435,691, representing amounts due the Lottery for tickets purchased by retailers. An allowance for doubtful accounts is reported as net of receivables and is based on historical perspective. As of March 31, 2007 the allowance is zero. An allowance for ticket returns is also included in the receivables amount. This allowance represents a reduction in receivables at March 31, 2007, for estimated ticket returns. This is an estimate based on returns received to date, as well as, an estimate of tickets unsold by retailers for games that have a public sale end date prior to April 1, 2007. The allowance for ticket returns is $2,512 at March 31, 2007. The return of vendor fees related to the allowance for returns is $145.

Inventories. Inventories consist of merchandise and supplies inventories. Merchandise inventory includes scratch tickets valued at $1,087,543 stored in the warehouse, at retailers prior to being activated by the retailer and with the marketing representatives. These ticket inventories are recorded at cost using the specific identification method and maintained on a perpetual inventory system. Tickets are charged to cost of tickets sold upon activation or after game end.

Supplies inventories include ticket dispensers, premiums and point-of-sale materials. At quarter end, supplies inventories totaled $112,788. These inventories are also recorded at cost using the specific identification method.

Other Current Assets. Other current assets consist of the following:

	March 31,	
	2007	2006
Prepaid Expenses	8,238	9,376
Employee Advances	0	3,825
TOTALS	$8,238	$13,201

Transfer Obligations. The account "Transfer Obligations" is $3,183,910 payable to the General Fund at March 31, 2007.

Compensated Absences. State employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Vacation leave may be accumulated not to exceed two times the maximum number of days earned annually. With no limit on accumulation, sick leave is earned at 12 days per year. Upon retirement or termination, an employee is paid 100% for unused vacation and 25% for unused sick leave. The Lottery's liability for compensated absences is detailed below.

Balance June 30, 2006	Net Leave Earned/(Used)	Balance March 31, 2007
$184,725	$6,025	$190,750

Commissions. Section 23-7-301(10), MCA, provides retailers a commission on scratch, Qwik Tix and lotto tickets or chances sold. The Lottery Commission established this commission at 5% of the face value of scratch tickets activated by the retailers and the face value of Qwik Tix and lotto tickets sold. In addition retailers can earn bonus commissions on tickets sold based on incremental sales of scratch tickets. For the quarter and nine months ended March 31, 2007 retailers earned bonus commissions of $95,889 and $291,293 respectively. For the quarter and the nine months ended March 31, 2007 total commissions were $660,913 and $1,884,854 respectively.

3. MARKETING PRODUCTION EXPENSES

The Lottery has contracted with several vendors to provide marketing related services and materials. These services include media placement, creative design and layout, and media production. Those services and materials not included in the Advertising and Advertising Production expense categories are printing and ticket dispensers. The cost of these services and materials, included in Operating Expenses as Contracted Services and Supplies and Materials, are detailed below for the nine months ended March 31, 2007:

Printing	$ 7,137
Ticket Dispensers	51,500
	$58,637

4. PAYMENTS TO OTHER STATE AGENCIES

The Lottery receives a variety of services and supplies and materials from other state agencies. These services and materials are detailed below for the nine months ended March 31, 2007:

Insurance	$13,899
Warrant Writing Services	743
Payroll Services	780
Audit Fees	7,614
Computer Fees	20,531
Printing	2,166
State Accounting System Support	8,354
Supplies and Materials	4,810
Mail Processing Fees	6,349
Telecommunications	13,820
Vehicle Rental Fees	1,073
Public Relations	0
Administrative Service Fees	40,510
SWCAP and SFCAP	1,693
Other	1,900
TOTAL	$124,242

5. PRIZES

Paid Prizes. Section 23-7-402, MCA states, "A minimum of 45% of the money paid for tickets or chances must be paid as prize money". Prize expense is recorded based on the predetermined prize structure percentage for each game less unclaimed prizes. For the quarter ended March 31, 2007, the prize expense of $5,901,213 is 52.25% of net Lottery ticket revenue of $11,293,861. For the nine

months ended March 31, 2007, the prize expense of $16,703,866 is 52.37% of net Lottery ticket revenue of $31,895,760.

6. TRANSFER TO STATE GENERAL FUND

Section 23-7-402(3), MCA, states "That part of all gross revenue not used for payment of prizes, commissions, and operating expenses, together with the interest earned on the gross revenue while the gross revenue is in the enterprise fund, is net revenue. Net revenue must be transferred quarterly from the enterprise fund established by 23-7-401 to the State General Fund." For the quarter ended March 31, 2007, the net revenue payable to the State General Fund totaled $3,183,910.

7. MULTI-STATE LOTTERY JOINT VENTURE

In November 1989 the Montana State Lottery joined the Multi-State Lottery Association (MUSL). MUSL was created in September 1987 to operate a multi-state lottery game for the benefit of party lotteries. Powerball, Wild Card, and Hot Lotto are the games jointly operated by the members, in which Montana presently participates. Each lottery participating in MUSL is represented on the Board of Directors.

The Multi-State Lottery Receivable with a balance of $1,486,396 as of March 31, 2007 is comprised of several reserve accounts, which are maintained by the Multi-State Lottery Association (MUSL). The balance of these reserve accounts is as follows:

Powerball Prize Reserve Account	$514,080
Powerball Set Prize Reserve Account	151,200
Powerball Unreserved Account	246,453
Wild Card Reserve Account	415,074
Hot Lotto Set Prize Reserve Account	159,589
TOTAL	$1,486,396

The Powerball Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Powerball game, assuming that no unanticipated prize claims have been paid. Interest earned on the Lottery's share of the fund, represented by the Unreserved Account, would be returned to the Lottery upon leaving MUSL. The amounts in the Unreserved Account may be used at the Board's discretion.

The Powerball Set Prize Reserve Account is used to fund prize payments for current drawings. Since the Powerball game has fixed prizes, it is often necessary to draw from this reserve to fund payment of prizes at the fixed amount. This account would be returned to the Lottery upon withdrawal from the Powerball Game.

The Lottery contributes to these reserve funds through the 50% set aside for prizes. In addition the Lottery was required to contribute for its portion of the reserve funds accumulated since the start of the Powerball game. The Lottery made this payment in full as of June 1990, through an additional 2% of drawing revenue rather than making a lump sum payment. Payments made to this fund are considered a portion of prize expense associated with the game.

The Wild Card Reserve Account is to be used in the event of an unanticipated prize claim on the Wild Card game. This account is also administered by MUSL and would be returned to the Lottery one year after the Wild Card Product Group of Idaho, Montana, South Dakota, and North Dakota is disbanded. The Lottery contributes to this account through the 55% set aside for prizes. Payments made to this fund are considered a portion of prize expense related to the Wild Card game.

The Hot Lotto Set Prize Reserve Account is administered by MUSL and is to be used only in the event of unanticipated prize claims. Like other MUSL games the reserve amount would be returned to the Lottery one year after withdrawal from the Hot Lotto game. The Lottery contributes to the reserve through the 50% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game.

8. GAMES

Currently, the Montana Lottery games are scratch ticket games, four lotto games referred to as Powerball, Montana Ca$h, Wild Card, and Hot Lotto and four instant play/instant win games referred to as Qwik Tix.

Scratch ticket games provide players the opportunity to win instantly by scratching a latex covering to reveal a prize.

The Powerball game allows players the chance to win a minimum pari-mutuel jackpot of approximately $15 million. A player must match all 6 numbers to win the jackpot; players win prizes ranging from $3 to $200,000 for matching less than all 6 numbers. Drawings are held twice weekly on Wednesday and Saturday nights. For any drawing, if no ticket matches 6 out of 6 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot. In March 2001, the Lottery added Power Play to the Powerball game. For an additional bet, the Power Play option provides non-jackpot winners the chance to multiply their prize amount by a factor of two through five.

The Montana Ca$h game allows players the chance to win a minimum pari-mutuel jackpot of $20,000. Players select 5 numbers from a field of 37 and must match at least 3 out of 5 to win a prize. Matching 3 of 5 wins $5 and 4 of 5 wins $200. The drawing is conducted twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot.

The Wild Card game allows players the chance to win a pari-mutuel jackpot, with a guaranteed minimum of $100,000. Players select 5 numbers from a field of 31 plus one of 16 face cards and must match all 5 numbers and the wild card to win the jackpot; players win prizes from $1 to $5,000 for matching less than all 5 numbers and/or the wild card. Drawings are held twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers and the wild card, the jackpot rolls over to the next drawing to create a progressive jackpot.

Hot Lotto allows players the chance to win a pari-mutuel jackpot with a guaranteed minimum of $1 million. Players choose 5 numbers from a field of 39 plus 1 Hot Ball number from a field of 19; the first 5 numbers and the Hot Ball must be matched to win the jackpot. Players can win prizes ranging from $2 to $10,000 by matching less than all 5 numbers and/or the Hot Ball. If no ticket wins the jackpot, it rolls over to the next drawing to create a progressive jackpot. Drawings are held twice weekly on Wednesday and Saturday nights.

Qwik Tix is a product line introduced by the Lottery in February 2004. There are four games, each with its own play style and prize structure. The four games are Lucky Numbers, a number match game; Hot Tac Toe, a tic tac toe grid; Jacks or Better, a poker game; and Montana Match, a match three symbols game. The Qwik Tix tickets are printed at the lotto terminal at the time of sale and can be redeemed immediately, with the maximum prize being $500. Each ticket costs $2 and consists of two plays of a single Qwik Tix game.

9. COMMITMENTS - GAMING SUPPLIER CONTRACTS

Scratch Tickets. On June 27, 2001 the Montana Lottery Commission approved the award of a one-year contract with Oberthur Gaming Technologies Corp. (Oberthur) for the provision of scratch tickets; the resulting contract was signed on August 8, 2001. The contract is for one year with the option for six additional one-year renewals. The contract contains specifications regarding ticket design, printing, game ownership, inspection, and prize structure.

Oberthur, as the vendor, provided a performance bond covering the contract term and an errors and omissions policy covering an ultimate net loss of $7,500,000. The Lottery may terminate this contract by providing proper notification to Oberthur.

On-line Services. On August 18, 1998, the Lottery signed a seven-year contract with Autotote Lottery Corporation to provide an on-line gaming system and associated services beginning March 28, 1999. The contract provides for payments to be made for the purchase of an on-line gaming system including terminals and software. The Lottery paid Autotote Lottery Corporation $5,025,311 for the system on April 26, 1999. Payment under the contract is also based on 8.35% of weekly Lottery sales. This contract expires on March 30, 2006.

On October 11, 2005, the Lottery signed a seven-year contract with Intralot, Inc. of Duluth, GA to provide an on-line gaming system and the associated services beginning March 31, 2006. The contract requires Intralot to provide new terminals to all retailers with the associated software and communications. Payment under the contract is based on 5.8% of net weekly Lottery sales. The contract provides for three one-year extensions, if agreeable by both parties.

10. CONTINGENT LIABILITIES - PRIZE ANNUITIES

During fiscal year 1989, the Montana Lottery awarded four Big Spin Jackpot prizes totaling $5,000,000. The Lottery made the initial payments to the winners in the amount of $253,088 and on September 26, 1988 the Montana Lottery awarded annuities in the amount of $2,350,180 to Western National Life. Through these annuities, Western National Life makes the remaining payments to the Big Spin Jackpot winners. The last payment for these annuities was made in February, 2007, so the contingent liability for future prize payments funded through the purchase of annuities is zero.

11. LOTTO*AMERICA/POWERBALL/TRI-WEST JACKPOT PRIZES

Jackpot prizes awarded in the Lotto*America/POWERBALL and TRI-WEST LOTTO games are funded through the purchase of U.S. Treasury Zero-Coupon Bonds purchased in the name of the Montana Lottery by MUSL. MUSL will cash the bonds each year as they mature and will wire the funds to the Lottery for payment to winners on the Anniversary date of the win.

On January 13, 1990 the Montana Lottery awarded its first Lotto*America jackpot prize totaling $1,740,000. The first annual payment of $87,000 was made on February 1, 1990. On May 9, 1990 the Lottery awarded a second Lotto*America jackpot prize of $3,000,000. The first annual payment of $150,000 was made on May 23, 1990. A third jackpot prize was awarded on February 2, 1991 for $7,360,000. The first annual payment of $368,000 was made February 15, 1991. On November 23, 1991 a fourth jackpot prize was awarded totaling $46,967,738.57. The first annual payment of $2,355,738.57 was made December 12, 1991. On April 11, 1992 a fifth jackpot prize was won totaling $2,000,000. The first annual payment of $100,000 was made on April 27, 1992.

On July 6, 1994 the Montana Lottery awarded its first Tri-West Lotto jackpot prize totaling $700,565. The first annual payment of $35,000 was made on July 26, 1994.

On July 22, 1995 the Montana Lottery awarded its first Powerball jackpot prize totaling $31,401,655.99. The first payment of $1,571,655.99 was made on August 8, 1995. On April 5, 1997 the Lottery awarded a second Powerball jackpot prize totaling $11,000,000. The first annual payment of $550,000 was awarded on April 18, 1997.

As of March 31, 2007 the combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Lotto*America winners was $11,620,739. The combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Powerball and Tri-West Lotto winners was $18,305,210.

On March 27, 1999 the Montana Lottery had a Powerball jackpot winner. The prize was $35.1 million ($19.35 million cash option). The winner chose the cash option and was paid a lump sum in June 1999.

12. LEASES

Rent. The Montana Lottery leases its office, administrative and warehouse facilities under a noncancelable lease agreement that is effective March 2002 through February 2007. This lease has been extended through August 2007. The monthly lease payments through August 2007 are $7,701.82.

13. INVESTMENT RISK DISCLOSURES

Effective June 30, 2005, the State of Montana implemented the provisions of Governmental Accounting Standards Board (GASB) Statement No. 40, *Deposit and Investment Risk Disclosures*. The Lottery participates in two investment pools: the Multi-State Lottery Association (MUSL) reserve accounts and the State of Montana's Short Term Investment Pool (STIP). There are four types of risk that must be disclosed. These risks are defined below, followed by their applicability to each of the investment pools.

Credit risk is defined as the risk that an issuer of an investment will not fulfill its obligation, i.e., not make timely principal and interest payments.

Custodial credit risk is the risk that the Lottery would not be able to recover the value of the investment or collateral securities that are in the possession of an outside party in the event of the failure of that party.

Concentration of credit is the risk of loss attributed to the magnitude of a government's investment in a single issuer.

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

Multi-State Lottery Association The MUSL investment policy for prize reserve and unreserved funds states that permitted investments "include direct obligations of the United States government, perfected repurchase agreements, and obligations issued or guaranteed as to payment of principal and interest by agencies or instrumentalities of the United States government, and mutual funds of approved investments". Obligations of the U.S. government or obligations explicitly guaranteed by the U.S. government are not considered to have credit risk nor concentration of credit risk per GASB Statement No. 40.

The securities are held in trust for MUSL by Mellon Trust. This large diversified institution was chosen to minimize custodial risk. It has several national offices, with the Everett, Massachusetts office handling the MUSL account. Interest rate risk is minimized by requiring that the average portfolio maturity be no more than 1.33 years and that the maximum maturity for any one security cannot exceed five years.

Short-term Investment Pool All short-term funds are held in the State's Short Term Investment Pool (STIP) administered by the Board of Investments (BOI). A summarized description of their disclosure follows and full details may be obtained by contacting the Montana Board of Investments, 2401 Colonial Drive, PO Box 200126, Helena, MT 59620-0126.

For STIP securities, BOI's policy to manage credit risk requires securities have the highest investment grade rating in the short-term category by at least one Nationally Recognized Statistical Rating Organization (NRSRO). The six NRSROs include Standard and Poors, Moody's, Duff and Phelps, Fitch, IBCA and Thompson's Bank Watch.

Per the BOI, all STIP securities are registered in the nominee name for the Montana Board of Investments and held in the possession of the Board's custodial bank. The STIP investment policy does not specifically address concentration of credit risk. However, as of June 30, 2005 there were no single issuer investments that exceeded 5% of the STIP portfolio. Per GASB Statement No. 40, interest rate disclosures are not required for STIP since STIP is a 2a-7-like pool.

Alternative accessible formats of this document will be provided upon request.